Office of Advocacy
www.sba.gov/advocacy

Advocacy: the voice of small business in government

Annual Report of the Office of Economic Research FY 2011

December 2011

Created by Congress in 1976, the Office of Advocacy of the U.S. Small Business Administration (SBA) is an independent voice for small business within the federal government. Appointed by the President and confirmed by the U.S. Senate, the Chief Counsel for Advocacy directs the office. The Chief Counsel advances the views, concerns, and interests of small business before Congress, the White House, federal agencies, federal courts, and state policy makers. Economic research, policy analyses, and small business outreach help identify issues of concern. Regional Advocates and an office in Washington, D.C., support the Chief Counsel's efforts.

For more information on the Office of Advocacy, visit **www.sba.gov/advocacy** or call (202) 205-6533. Receive email notices of new Office of Advocacy information by signing up on Advocacy's Listservs at **http://web.sba.gov/list**.

☑ **ADVOCACY NEWSLETTER**
☑ **ADVOCACY PRESS**
☑ **ADVOCACY REGULATORY NEWS**
☑ **ADVOCACY RESEARCH**

Cover illustration from Thinkstock.com

Foreword

We are pleased to provide this FY 2011 annual report for the Office of Advocacy's Office of Economic Research (OER). The Office of Advocacy continues to stress the importance of sound economic research that will provide our small business stakeholders with timely and actionable information about the current economic climate.

The legislation that authorized the Small Business Administration's Office of Advocacy, Public Law 94-305, highlighted economic research as a core mission of the office. The law assigned to Advocacy the task of examining "the role of small business in the American economy and the contribution which small business can make in improving competition."

With the recession and financial meltdown that began in 2007 and the ongoing challenge small businesses face in raising needed capital, Advocacy's Office of Economic Research in fiscal year 2011 decided to take a hard, in-depth look at the state of the economy, small business job creation, and small business access to financing. In fiscal year 2011, beginning October 1, 2010, our Office of Economic Research produced 25 separate contract and internal research reports about topics ranging from small business innovation and job creation to the demographics of business ownership, health care costs, and tax burdens.

In addition to these reports, Advocacy convened research conferences in FY 2011 on job creation and access to capital. These outreach efforts are important for small business stakeholders here in Washington. It is also important—always, and especially in the current economic climate—to hear from the small business community outside of Washington, D.C.

We appreciate our stakeholders' contributions in support of the best possible research on small business and we look forward to hearing from you in the year ahead. For more information about the Office of Advocacy, visit our website at www.sba.gov/advocacy.

Winslow Sargeant, Ph.D.
Chief Counsel for Advocacy

Joseph M. Johnson, Ph.D.
Director, Office of Economic Research

Contents

Introduction

In fiscal year 2011, the Office of Advocacy continued to offer timely research on a variety of small business topics, from capital formation to the demographics of small business ownership. However, given the state of the economy and the importance of the small business role in it, two topics emerged as the most pressing areas for a research focus: financing and small business job creation.

Advocacy's research has long shown the importance of small businesses in creating new jobs. Research reports in many formats, including the *Frequently Asked Questions* (FAQ), have documented the fact that small firms created some two-thirds of all the net new jobs beginning in the early 1990s. By the end of the first decade of the 21st century, it was clear that small business job creation was lagging, and it appeared that lack of access to financing was an important part of the problem.

In response to the pressing need for new and timely information on these topics, Advocacy's Office of Economic Research (OER) began several initiatives in FY 2011. OER's research offers help for small business stakeholders in several forms: research produced by contractors with special expertise in particular databases or subject areas, in-house research by Advocacy's team of economists, and the provision of data on small businesses and their role in the economy available via Advocacy's website.

In FY 2011, Advocacy began an effort to make its research products more reader-friendly and electronically accessible. The *Frequently Asked Questions* document was updated. *Quarterly Indicators: The Economy and Small Business* became a newly formatted and updated *Small Business Quarterly Bulletin*. With a specific focus on small business financing, two new recurring publications were added: *Frequently Asked Questions about Finance* and a second quarterly report, the *Quarterly Lending Bulletin*. The new publications have been well received and widely read by Advocacy stakeholders.

The Office of Advocacy partners with the U.S. Census Bureau to collect and report important data on small business. Advocacy economists process and analyze the data to produce easy-to-understand statistical tables and reports downloadable from Advocacy's website. Data on businesses with employees and associated business characteristics are from the Statistics of U.S. Businesses, Business Dynamics Statistics, and Business Employment Dynamics. Data on nonemployers are from the Nonemployer Statistics program. The data programs are administered by the U.S. Census Bureau, except the Business Employment Dynamics data series from the U.S. Bureau of Labor Statistics.

Beyond research products, the Office of Advocacy convened two national conferences in fiscal year 2011 to reach out to small business stakeholders for both input on these topics and dissemination of research results. Shortly after a FY 2010 conference on the Regulatory Flexibility Act, Advocacy sponsored its first FY 2011 conference, "High-Impact Entrepreneurship Outlook: Finance and Innovation Create Jobs." Late in the fiscal year, on September 15, 2011, Advocacy revisited the need for both debt and equity financing and proposed solutions in a symposium, "The Small Business Capital Crunch: Debt and

Equity." In addition to these Washington-based symposia, a series of regional roundtables during the fiscal year looked at women-owned small business contributions to the economy. The Chief Counsel also participated in a number of roundtables highlighting Advocacy research, as well as the office's role in regulatory flexibility.

In a variety of ways, Advocacy's Office of Economic Research in FY 2011 continued to advance the mission of providing small business research that is timely and relevant for use by the many stakeholders interested in small business contributions to the U.S. economy.

Advocacy Research Reports, FY 2011

In FY 2011, Advocacy's Office of Economic Research produced 25 reports on topics ranging from federal tax compliance burdens to entrepreneurship among veterans and women. This section lists OER's FY 2011 research reports by release date, beginning with the latest. Visit the Office of Advocacy website for research reports available online: **http://www.sba.gov/advocacy/7540/**.

- ***Developments in Women-owned Businesses, 1997-2007***
  http://www.sba.gov/advocacy/7540/26381
  Release date: September 29, 2011
  Author: Dr. Ying Lowrey
  Based on data from the Survey of Business Owners, this study looks at how women and other small business owners fared during the ten-year period, 1997-2007. The study finds that 12 percent of women business owners had employees in 2007, while 88 percent did not. Women-owned firms employed 6.4 percent of the 118.6 million employees of employer firms in 2007. The top four sectors for employer firms owned by women were retail trade, professional services, health care and social assistance and accommodations.

- ***Regional Roundtables Focused on Women-owned Business***
  http://www.sba.gov/sites/default/files/Womens_roundtable_summary.pdf
  Release date: September 29, 2011
  Author: Office of Advocacy
  The Office of Advocacy released a summary of the results of roundtables held in the last week of June 2011 in each of the ten SBA regions. The events, convened by Advocacy's Regional Advocates, brought together women from all walks of life to discuss the challenges women-owned businesses face, as well as their successes. The roundtables were held in Maine, New York, Pennsylvania, Georgia, Wisconsin, Louisiana, Iowa, Colorado, California, and the state of Washington. Participants included women business owners and various leaders of women's organizations, as well as government employees.

- ***The Increasing Importance of Credit Unions in Small Business Financing***
  http://www.sba.gov/advocacy/7540/23691
  Release date: September 14, 2011
  Author: James A. Wilcox
  The study examines annual state-level data and national aggregate data for banks and credit unions from 1986 to 2010 and finds that, even during the financial crisis, credit unions may have provided some extra business lending in response to reductions in business lending by banks.

- ***Bank Liquidity Pressures and the Availability of Bank Credit to Small Firms: Was the 2007-2009 Credit Crisis Different?***
  http://www.sba.gov/advocacy/7540/23701
  Release date: September 14, 2011
  Author: Joe Peek
  With respect to the availability of bank credit to small firms, the study finds that the liquidity of bank assets became an important factor in the financial crisis, as healthier banks tended to shy away from small commercial and industrial and small commercial real estate loans.

- ***Measuring and Modeling the Federal Income Tax Compliance Burden of Small Businesses***
  http://www.sba.gov/advocacy/7544/24761
  Release date: September 13, 2011
  Author: Quantria Strategies
  This study on the federal tax compliance burden for small firms found that the burden of complying with federal income tax requirements is of particular concern to American small businesses. Compliance burdens increase as the size of a small business increases and vary by industry and other factors, the study shows.

- ***Frequently Asked Questions about Small Business Finance***
  http://www.sba.gov/advocacy/9601
  Release date: September 8, 2011
  Author: Victoria Williams
  Advocacy's new Finance FAQ explores questions of how small businesses are financed in a useful, concise format. The Finance FAQ looks at both the debt and equity aspects of the small business balance sheet. Small businesses borrow for four principal reasons: starting a business, purchasing inventory, expanding, and strengthening the firm's financials. The Finance FAQ is replete with data about where small businesses obtain their financing, including 15 graphs showing types of startup and expansion financing, as well as trends in bank lending, interest rates, venture capital, initial public offerings, SBIC funding, and SBA loans.

- ***Health Insurance in the Small Business Market: Availability, Coverage, and the Effect of Tax Incentives***
  http://www.sba.gov/advocacy/7540/22181
  Release date: September 2, 2011
  Author: Quantria Strategies
  Advocacy published significant new research on the availability and coverage of health insurance in the small business market. The researchers examined whether existing tax incentives at the state and federal levels provide sufficient inducement to small businesses to adopt health insurance plans. They found no correlation between state tax rates and state insurance offer rates by size of firm. They also found that approximately 2.6 million of the 4 million firms estimated to be eligible for the health insurance tax credit in the 2010 federal legislation would have received a benefit from the credit in 2010.

- ***Small Business Quarterly Bulletin, Second Quarter 2011***
  http://www.sba.gov/advocacy/7540/15150
  Release date: August 2011
  Author: Brian Headd
  Advocacy's Small Business Quarterly Bulletin for the second quarter of 2011 contains commentary and analysis on the current employment and financing trends of small businesses, and shows a continuing but uneven climb for small businesses in second quarter 2011 from the depths of the recession. Small business demand for loans increased in both of the first two quarters and the number of startups is increasing.

- ***Accelerating Job Creation in America: The Promise of High-Impact Companies***
  http://www.sba.gov/advocacy/7540/17211
  Release date: July 2011
  Author: Spencer Tracy
  This report explores the contributions of high-impact companies to job creation. A previous Advocacy-funded study from Corporate Research Board, *High-Impact Firms: Gazelles Revisited*, found that fast-growing or high-impact companies were a main contributor to new jobs. In light of the current need for a growing labor market, a natural question is how the deteriorating economy of 2008 affected high-impact companies and their jobs. This study picks up where the previous one left off and addresses such additional questions as the gender of the owners and the financial condition of high-impact companies.

- ***Quarterly Lending Bulletin / Small Business Lending: First Quarter 2011***
  http://www.sba.gov/sites/default/files/files/SBL_2011Q1.pdf
  Release date: June 2011
  Author: Victoria Williams
  Advocacy's *Quarterly Lending Bulletin* presented a brief analysis of the current small business lending situation and showed a drop in loans outstanding to small businesses during the first quarter of 2011 compared with the previous quarter. Total business loans outstanding and gross domestic product continued to trend upward.

- ***Small Business Quarterly Bulletin, First Quarter 2011***
  http://www.sba.gov/sites/default/files/files/SBQB_2011q1.pdf
  Release date: May 26, 2011
  Author: Brian Headd
  The *Small Business Quarterly Bulletin*, a new publication with commentary and analysis on the current employment and financing trends of small businesses, showed a positive first quarter 2011 for small businesses. Small business employment and financing were trending upward along with GDP, which had been growing for seven quarters.

Factors Affecting Entrepreneurship among Veterans
http://www.sba.gov/advocacy/7540/15428
Release date: May 11, 2011
Author: SAG Corporation
This report took a new look at veteran entrepreneurship. Previous Advocacy-sponsored research and more than three decades of data from the Bureau of Labor Statistics have established that veterans have a consistently higher rate of self-employment than nonveterans. Why? The new study investigates this question and quantifies a variety of factors observed in its analyses.

How Do Firms Choose Legal Form of Organization?
http://www.sba.gov/sites/default/files/files/rs383tot.pdf
Release date: April 20, 2011
Author: Rebel Cole
To incorporate, or to not to incorporate: that is the question posed at start-up. This report finds that the choice of legal form of organization is relatively stable over a firm's first four years. When changes do occur, they tend to be to the more complex forms of organization.

Beyond Bankruptcy: Does the Bankruptcy Code Provide a Fresh Start to Entrepreneurs?
http://www.sba.gov/advocacy/7540/15050
Release date: April 6, 2011
Author: Aparna Mathur
The U.S. bankruptcy system is designed to recover funds for creditors while giving bankrupt small businesses an opportunity for a "fresh start." While a fresh start is a goal of the system, little analysis has been done to evaluate the ability of small firms to reset and thrive after bankruptcy. This paper attempts to fill that gap. The research finds that 2.6 percent of firms filed for bankruptcy within the previous seven years, that they are comparable to other firms in terms of cash flow and firm size, and that they have a 24 percent higher likelihood of being denied a loan and are charged interest rates 1 percent higher than those charged other firms.

Quarterly Lending Bulletin / Small Business Lending: Fourth Quarter 2010
http://www.sba.gov/sites/default/files/files/SBL_2010Q4.pdf
Release date: March 28, 2011
Author: Victoria Williams
The Office of Advocacy issued its first *Quarterly Lending Bulletin*, a new report summarizing trends in small business lending based on Call Report data. Analysis of bank holding companies and other depository institutions with assets over $50 billion indicated that small business loans outstanding had stabilized since the previous September. Overall, small business lending outstanding appeared to be stabilizing compared with the trend in the previous quarter. However, the general results showed that aggregate small business lending had yet to follow the trend of gross domestic product (GDP) which had turned upward, along with total business lending.

Lending by Depository Institutions to Small Businesses, 2003-2010
http://www.sba.gov/advocacy/7540/14927
Release date: March 24, 2011
Author: George Haynes
This study examined the supply of small business lending from depository lenders over the 2003-2010 period. The study used five performance measures: small business aggregate loan volume, numbers of loans, average loan sizes, and ratios of small business loans to total assets and of small business loans to total business loans. The research relied on data provided by depository institutions to their respective regulating agencies—Call Reports for June of each year from 2003 to 2010. The first section emphasized lending institutions with total assets exceeding $10 billion, while the second examined small business loans held by "community lenders" with assets of less than $10 billion. Small businesses continued to rely heavily on large banks for capital: the largest lenders with more than $50 billion in assets increased their market share of small business lending from 28.7 percent in 2003 to 38.7 percent in 2010.

An Examination of the 2001 IRS Tax Gap Estimates' Effects on Small Businesses
http://www.sba.gov/advocacy/7540/14864
Release date: March 23, 2011
Author: Quantria Strategies
The study shows that small businesses are disproportionately affected by measures to close the tax gap—the difference between taxes owed and taxes paid. The study highlights flaws with the overall estimates, particularly as they relate to large corporations and international tax transactions.

2010 Small Business Profiles for the States and Territories
http://www.sba.gov/advocacy/7540/14513
Release date: February 28, 2011
Author: Victoria Williams, Rebecca Krafft, ed.
The small business profiles supply data on small firms in each of the 50 states and the District of Columbia, as well as national-level data and limited data on the U.S. territories. The following topics are covered: the number of firms, demographics of business ownership, small business income, banking, business turnover, industry composition, and employment gains and losses by size of business.

Small Business Lending in the United States, 2009-2010
http://www.sba.gov/advocacy/7540/14432
Release date: February 10, 2011
Author: Victoria Williams and George Haynes
The study used Call Reports for 2010 and Community Reinvestment Act (CRA) reports for 2009 to examine the lending activities of U.S. depository institutions. The data cover savings banks and savings and loan associations, in addition to commercial banks. Geographic coverage includes the 50 states and the District of Columbia, American Samoa, Guam, Puerto Rico, and the U.S. Virgin Islands. This edition for the first time includes cooperative banks. The rankings and performance of these lenders were summarized and

organized by state/ territory, loan size, number of loans, and asset size of the institution. Lending to small firms by U.S. financial institutions continued to decline, but began to stabilize in some loan size categories over the 2009-2010 period. GDP has turned upward, and business lending may follow the pattern of other recessions, in which commercial and industrial lending grew only after the recovery was well under way.

The Small Business Economy 2010
http://www.sba.gov/advocacy/7540/13789
Release date: January 25, 2011
Author: Advocacy Office of Economic Research, Kathryn Tobias, ed.
The 2010 edition of *The Small Business Economy* featured subsections on small business contributions to job creation and innovation, challenges such as health care and pension coverage, and opportunities in exporting and federal procurement. The report showed that in 2009, after weathering a deep recession that began in late 2007, the American economy began to stabilize. For small businesses, one of the biggest remaining challenges was the lack of sales adequate to grow employment. Many economic indicators began to show improvement by year's end.

Frequently Asked Questions about Small Business (FAQ)
http://www.sba.gov/advocacy/7495
Release date: January 2011
Author: Brian Headd
Frequently Asked Questions about Small Business gathers dozens of the latest statistics about America's small business in one place. Updated annually, it is a convenient source for confirming facts like the total number of small businesses, their share of employment and net new jobs, starts, closures, and small firms' overall contribution to the U.S. economy.

Small Business Lending in the United States, 2008-2009
http://www.sba.gov/advocacy/7540/12979
Release date: December 10, 2010
Author: Victoria Williams
The report used June 2009 Call Report data and 2008 Community Reinvestment Act data to examine developments in small business lending in 2008-2009. It provided a listing of the top small and micro business lenders in the 50 states, the District of Columbia, and some U.S. territories. The report found that lending and borrowing by lending institutions and small firms declined in response to uncertain economic conditions in 2008-2009. For the first time since the Call Reports became available in 1994, lending in all loan size categories declined. The drop was most severe in the market for loans under $100,000, as borrowers and lenders held off on new lending activity.

The Impact of Broadband Speed and Price on Small Business
http://www.sba.gov/advocacy/7540/12828
Release date: November 16, 2010
Author: Columbia Telecommunications Corporation
This report was a congressionally mandated study of businesses' Internet access across the nation. The authors developed a framework to evaluate the options available to small businesses, rural and urban, and conducted a survey of business Internet usage and costs. A key finding is the difference in the price and speed of broadband service available in rural and urban America. When prices were held constant, rural small businesses received less service than metropolitan small businesses; when services were held constant, rural small businesses paid higher prices than urban small businesses.

Quarterly Indicators: The Economy and Small Business
http://archive.sba.gov/advo/research/sbqei1003.pdf
Release date: November 10, 2010
Author: Chad Moutray
This update of Advocacy's series on small business economic trends showed that the U.S. economy grew for the fifth consecutive quarter, with real gross domestic product up 2 percent in the third quarter. Personal consumption, which makes up 70 percent of real GDP, increased at a 2.6 percent annual rate. Real gross private fixed investment was up an annualized 12.8 percent, and real exports rose 5 percent.

Race/Ethnicity and Establishment Dynamics, 2002-2006
http://www.sba.gov/advocacy/7540/12158
Release date: November 5, 2010
Author: Ying Lowrey
This report matched data from the 2002 Survey of Business Owners (SBO) and the 1989-2006 Business Information Tracking Series (BITS). The series focused on business dynamics by gender, race/ethnicity, and business type (publicly or non-publicly held). The report first provides general social, economic, and business background by race/ethnicity of the owner. The report also covers the industry, employment, and/or receipts size, and state location characteristics of establishments (those with employees) for which the race/ethnicity of the enterprise owner was identified in 2002.

Research Conferences

In light of the recession's effects on small firms, which continue to be the nation's foremost job creators, the Office of Advocacy sponsored two conferences in fiscal year 2011 looking at small firms' job creation role and the need for better access to capital for all small firms, especially those prolific "high-impact" creators of innovative products and jobs.

High-impact Entrepreneurship Outlook: Finance and Innovation Create Jobs

On October 14, 2010, Advocacy gathered small business stakeholders on Capitol Hill for a symposium on how and what kinds of jobs innovative small businesses create, as well as the current state of small business finance. Topics for discussion included:

- Where we are in the early 21st century: A look at the kinds of high growth firms that have been creating jobs.
- The importance of innovation and incentives: The critical roles of innovative ideas and the tangible and intangible economic factors that encourage them.
- Financing high-impact firms: Can financial incentive structures be changed to better support entrepreneurial firms?

The day was designed to allow for maximum audience participation. Members of the small business community, economists, and policymakers joined SBA Administrator Karen Mills and Advocacy Chief Counsel Winslow Sargeant for discussions and a networking opportunity. The consensus of many participants was that public-private partnerships are important in helping small businesses succeed and create jobs. Speaker Dr. Jeremy Wiesen pointed out that the U.S. government funded the Internet, known as Arpanet, in the 1960s, and provided grants that led to key private sector breakthroughs in semiconductor technology. Government actions have often been a catalyst for private sector innovation and subsequent job creation.

SBA Administrator Karen Mills summed up key measures in the Small Business Jobs Act, which provided $30 billion in funding to community banks, intended as a lifeline for small businesses and a catalyst for further capital infusions. Gene Sperling, counsel to the Secretary of the Treasury, closed the symposium with more details on the act. The high-level officials in attendance signaled the importance of the small business job creation and financing topic to the Administration and the nation.

Small Business Capital Crunch: Debt and Equity

Following up on findings that small firms were struggling to gain access to the capital they need to start and grow their businesses, the Office of Advocacy convened a symposium on September 15, 2011, on debt and equity aspects of the small business financing challenge.

The event at the Capitol Visitors Center also provided participants with new Advocacy research tools, including the publication, *Frequently Asked Questions about Small Business Finance* and two new research studies, *Bank Liquidity Pressures and the Availability of Bank Credit to Small Firms: Was the 2007-2009 Credit Crisis Different?* and *The Growing Impact of Credit Unions on Small Business Lending*.

Chief Counsel Winslow Sargeant opened the conference. The first panel, "How to Fix the Banking Crunch," brought together an economist, a banker, and a small business owner for their perspectives on the capital crunch in the banking sector.

- Federal Reserve Board research economist Traci Mach discussed the numbers behind the capital crunch in the banking sector. Based on call report data, small business loans continued to decline in the second quarter, while large business loans picked up.
- Jim Chessen of the American Bankers Association focused on the landscape for banks—most of them small—and said that Dodd-Frank has seriously added to the regulatory burden for small banks.
- Marilyn Landis of Basic Business Concepts, Inc., provides CFO-level services to small businesses, and said that for small firms struggling with the downturn, the greatest need for capital is in amounts under $250,000.

The second panel assembled three experts to look at the equity side of the capital crunch.

- Daphne Dufresne, who has worked in the venture capital and private equity business, said that in the lower middle market—companies with cash flow of $6 million to $15 million—equity infusions have led to increases in jobs and growth.
- Mark Heesen, president of the National Venture Capital Association, discussed the ongoing partnership that accompanies equity financing.
- David Robinson, professor of finance at Duke University's Fuqua School of Business, said that while venture capital-backed firms are a very small fraction of the number of small firms, they account for a disproportionate share of job growth.

Closing the conference, Chief Counsel Winslow Sargeant noted that while one year is a data point to an economist, to a small business owner it is 365 mornings of waking up to concerns about the business. Those who will create the next great companies will need the capital to start and grow.

Data Access

In fiscal year 2011, the Office of Advocacy continued to provide downloadable data and links to data on its website. Data cover businesses with and without employees—employer and nonemployer firms.[1] Most firms are nonemployer firms; the larger share of receipts and payroll are in employer firms.

Data on employers and associated business characteristics are from the Statistics of U.S. Businesses (SUSB), Business Dynamics Statistics (BDS), and Business Employment Dynamics (BED) programs and data on nonemployers are from the Nonemployer Statistics (NE) program. The data programs are annual and are produced by the U.S. Census Bureau, except the Business Employment Dynamics data series, which is quarterly, from the U.S. Bureau of Labor Statistics. Detailed data on business owners and business characteristics are available from the U.S. Census Bureau's Survey of Business Owners, part of the Economic Census, for years ending in 2 or 7.

The PDF files on Advocacy's website present quick views of data at high levels of aggregation and are available in MS Excel files for ease of use. The tab-delimited text files contain more data detail and can easily be copied and pasted into spreadsheet software.

Public and federal agencies are encouraged to use the data for economic research and regulatory analyses. The Office of Advocacy defines a small business for research purposes as an independent business having fewer than 500 employees.[2]

Differences Between Static and Dynamic Data

Most of the tables use static data, which indicate the importance of firm size classes and their changing importance over time. Dynamic data indicate the growth of firm size classes over time. Dynamic data were created using a longitudinal database from the U.S. Census Bureau.

Static firm size data report the number of firms, number of establishments, employment, annual payroll, and estimated receipts by employment size of firm. Firms are defined by their employment size at a point in time on a yearly basis. Because firms can change employment size classes from year to year, static firm size data cannot indicate the performance of employment size classes. However, comparisons of static firm size data can illustrate the changing importance of small and large firms by location or industry.

1 See **http://www.sba.gov/advocacy/849/12162**.

2 Note, however, that for purposes such as government contracting and lending, the SBA's Office of Size Standards provides detailed industry definitions of small businesses.

Dynamic firm size data report changes in establishments and employment classified by the beginning year employment size of a firm. Changes are caused by the creation of new firms (original establishments) or new establishments of existing firms (secondary establishments), deaths of original or secondary establishments, and expansion or contraction of employment at existing establishments. New firms are classified by their end-of-year firm size. Dynamic data show the performance of firm employment size categories.

Dynamic and static figures can differ because dynamic data exclude establishments with zero employment. End-of-year figures in firm employment size categories will differ between dynamic and static data for the same year because in dynamic data, firms are defined by their beginning year employment size. Dynamic data are better than static data for tracking firms that change in ownership or legal form during the year.

Statistics of U.S. Businesses

The Office of Advocacy partially funds the U.S. Census Bureau to produce data on employer firm size in the Statistics of U.S. Businesses (SUSB) program. In these data, a firm is defined as the aggregation of all establishments owned by a parent company (within a geographic location and/or industry) that have some annual payroll. A firm may be located in one or more places.

SUSB's employer data include the number of firms, number of establishments, employment, and annual payroll for employment size of firm categories by location and industry. The employer data consist of static and dynamic data. Unless otherwise noted, the data are static, that is, they are a "snapshot" of firms at a point in time. Receipts by employment size of firm are available for 1997 and 2002, and special tabulations by receipts size of firm are available for the United States. Industries are defined according to Standard Industrial Classification for 1988 to 1998 and the North American Industry Classification System (NAICS) thereafter.

Data include the following, most by employment size class:
- The economy segmented into 25 size classes, 2008 (PDF file) 1992-2008 (TXT file)
- Totals, 1988-2008 (PDF file)
- Major industries, 1988-1998, 1998-2008 (PDF files)
- All industries by NAICS codes, 2008 (PDF file)
- All industries, 1990-1998, 1998-2002, 2003-2008 (TXT files)
- Legal form of organization by major industry, 2008 (PDF file)

Classified by other firm size measures:
- Receipts size of firm by major industry group, 1997, 2002 & 2007 (PDF file)
- All industries by receipts size, 1997, 2002, 2007 (TXT files)
- Annual payroll size of firm by major industry group, 2006 (PDF file)

Dynamic data, by births, deaths, growth, and decline:
- Business births, deaths and job creation, 1989-2008 (PDF file)
- Major industries, 2005-2008 (PDF file)

- Industry data, 1989-1998, 1998-2008 (TXT files)

State, Metropolitan Statistical Area (MSA) and county (Microsoft Excel file of PDF files plus historic data)

Classified by employment size of firm:

- State totals, 1990,1995, 2000-2008 (PDF file) 1988-2008 (TXT File)
- State major industry data, 1988-1997, 1998-2002, 2003-2008 (TXT file)
- State detailed industry data, 1998-2008 (TXT file)
- MSA totals, 1995, 2000-2008 (PDF file)
- MSA major industry group data, 2004, 2005, 2006, 2007, 2008, Totals 1993-2008 (TXT files)
- State MSA and Non-MSA totals, 1995-2008 (TXT file)
- Micropolitan Statistical Areas 2004, 2005, 2006, 2007, 2008 (TXT file)
- Counties: size class 2007-2008, totals 2000-2008 (TXT files)

Classified by annual payroll size of firm:

- State annual size of firm, 2006 (PDF file)

Dynamic data, births, deaths, growth and decline:

- State totals, 2005-2008 (PDF file)
- State MSA/ Non-MSA net changes, 2005-2008 (PDF file)
- MSA business births, deaths and employment, 2005-2008 (PDF file)
- State major industry data 1989-1998, 1998-2008 (TXT files)
- State MSA and non-MSA totals, 1995-2008 (TXT file)
- Metro and micropolitan statistical areas, 2003-2008 (TXT file)
- Counties (no size data available), 2005-2007, 2007-2008; (TXT file)

Business Dynamics Statistics

Business Dynamics Statistics (BDS) provide employer firm data by firm age.[3] Advocacy's website offers an introduction to the data program including the following:[4]

- Firms and establishments by firm age, 1977-2009 (Microsoft Excel file)
- Employment by firm age, 1977-2009 (Microsoft Excel file)
- Establishments and employment by employment size of firm, 1977-2009 (Microsoft Excel file)

3 For more information see Business Formation and Dynamics by Business Age: Results from the New Business Dynamics Statistics by John Haltiwanger, Ron Jarmin and Javier Miranda, **http://www.ces.census.gov/docs/bds/bds_paper_CAED_may2008_dec2.pdf.**

4 More information can be found on the U.S. Census Bureau's Business Dynamics Statistics program website at http://www.ces.census.gov/index.php/bds and on the database list at for background about the data and their database list at **http://www.ces.census.gov/index.php/bds/bds_database_list**.

Business Employment Dynamics

The Business Employment Dynamics program offers employer firm data with a focus on employment changes from establishment entry, growth, decline, and exit. Because the data are quarterly, some establishments close and reopen in the same year. Fortunately, BLS presents the data in two ways to capture the seasonal firms by listing establishment openings (establishments that did not exist in the previous quarter) and establishment births (those that did not exist in the previous year), with similar classifications for business closings and deaths.[5] Recently, the data program has added establishment age data. Advocacy's website introduces the data program; the U.S. Department of Labor, Bureau of Labor Statistics' BED program provides background and more detailed data.[6] Data provided include the following:

- Quarterly establishment births, deaths and associated employment, mid-1992–2010
- State quarterly establishment births, deaths and associated employment, mid-1992–2010 (see Tables 9)
- Quarterly net job change by employment size of firm, mid-1992–2010 (totals do not match other figures as some firms do not have firm size identifiers)
- Employer firms by employment size of firm, 1993–2010
- Employment by employment size of firm, 1993–2010
- Establishment age and survival 1994–2010
- Establishment size of change (**www.bls.gov/bdm/bdsoc.htm**)

Nonemployer Statistics

A nonemployer firm is defined as one that has no paid employees, has annual business receipts of $1,000 or more ($1 or more in the construction industries), and is subject to federal income taxes. The Census Bureau, which provides nonemployer business data, finds that "Nonemployers account for roughly 3 percent of business activity [in terms of sales or receipts]. At the same time nonemployers account for nearly three-quarters of all businesses. Most nonemployer businesses are very small, and many are not the primary source of income for their owners."[7] The following data are included:[8]

- U.S. industry data by NAICS code, 1997-2009 (PDF file)
- State totals, 1992,1997-2009 (PDF file)
- Capital expenditures for employers and nonemployers, 1996-2009 (PDF file)

5 For more information, see Measuring job and establishment flows with BLS longitudinal microdata by Timothy Pivetz, Michael Searson, and James Spletzer for information on the data program.

6 See **http://www.bls.gov/bdm/**.

7 For details, see the U.S. Census Bureau's Nonemployer Statistics at **http://www.census.gov/econ/nonemployer/** and the Annual Capital Expenditures Survey at **http://www.census.gov/econ/aces/**.

8 For county data, go directly to the U.S. Census Bureau's Nonemployer Statistics, **http://www.census.gov/econ/nonemployer/**.

Appendix A: Research Functions

Public Law 94-305: Research Functions of the Office of Advocacy

Public Law 94-305 established the Office of Advocacy within the U.S. Small Business Administration and included a list of Advocacy's primary functions codified in 15 U.S.C. § 634b. Paragraph 11 was added to the list by P.L. 96-481 in 1980 and paragraph 12 was added by P.L. 106-50 in 1999.

15 U.S.C. § 634b: Primary functions of Office of Advocacy

The primary functions of the Office of Advocacy shall be to—

(1) examine the role of small business in the American economy and the contribution which small business can make in improving competition, encouraging economic and social mobility for all citizens, restraining inflation, spurring production, expanding employment opportunities, increasing productivity, promoting exports, stimulating innovation and entrepreneurship, and providing an avenue through which new and untested products and services can be brought to the marketplace;
(2) assess the effectiveness of existing Federal subsidy and assistance programs for small business and the desirability of reducing the emphasis on such existing programs and increasing the emphasis on general assistance programs designed to benefit all small businesses;
(3) measure the direct costs and other effects of government regulation on small businesses; and make legislative and nonlegislative proposals for eliminating excessive or unnecessary regulations of small businesses;
(4) determine the impact of the tax structure on small businesses and make legislative and other proposals for altering the tax structure to enable all small businesses to realize their potential for contributing to the improvement of the Nation's economic well-being;
(5) study the ability of financial markets and institutions to meet small business credit needs and determine the impact of government demands for credit on small businesses;
(6) determine financial resource availability and to recommend methods for delivery of financial assistance to minority enterprises, including methods for securing equity capital, for generating markets for goods and services, for providing effective business education, more effective management and technical assistance, and training, and for assistance in complying with Federal, State, and local law;
(7) evaluate the efforts of Federal agencies, business and industry to assist minority enterprises;
(8) make such other recommendations as may be appropriate to assist the development and strengthening of minority and other small business enterprises;

(9) recommend specific measures for creating an environment in which all businesses will have the opportunity to complete [compete] effectively and expand to their full potential, and to ascertain the common reasons, if any, for small business successes and failures;
(10) determine the desirability of developing a set of rational, objective criteria to be used to define small business, and to develop such criteria, if appropriate;
(11) advise, cooperate with, and consult with, the Chairman of the Administrative Conference of the United States with respect to section 504(e) of title 5; and
(12) evaluate the efforts of each department and agency of the United States, and of private industry, to assist small business concerns owned and controlled by veterans, as defined in section 632(q) of this title, and small business concerns owned and controlled by serviced-disabled [service-disabled] veterans, as defined in such section 632(q) of this title, and to provide statistical information on the utilization of such programs by such small business concerns, and to make appropriate recommendations to the Administrator of the Small Business Administration and to the Congress in order to promote the establishment and growth of those small business concerns.

APPENDIX B
Frequently Asked Questions

Advocacy: the voice of small business in government

What is a small business?

The Office of Advocacy defines a small business as an independent business having fewer than 500 employees. (The definition of "small business" used in government programs and contracting varies by industry; see **www.sba.gov/size**.)

How important are small businesses to the U.S. economy?

Small firms:

- Represent 99.7 percent of all employer firms.
- Employ about half of all private sector employees.
- Pay 43 percent of total U.S. private payroll.
- Have generated 65 percent of net new jobs over the past 17 years.
- Create more than half of the nonfarm private GDP.
- Hire 43 percent of high tech workers (scientists, engineers, computer programmers, and others).
- Are 52 percent home-based and 2 percent franchises.
- Made up 97.5 percent of all identified exporters and produced 31 percent of export value in FY 2008.
- Produce 16.5 times more patents per employee than large patenting firms.

Source: U.S. Dept. of Commerce, Census Bureau and Intl. Trade Admin.; Advocacy-funded research by Kathryn Kobe, 2007 (**archive.sba.gov/advo/research/rs299tot.pdf**) and CHI Research, 2003 (**archive.sba.gov/advo/research/rs225tot.pdf**); U.S. Dept. of Labor, Bureau of Labor Statistics.

How many small businesses are there?

In 2009, there were 27.5 million businesses in the United States, according to Office of Advocacy estimates. The latest available Census data show that there were 5.9 million firms with employees in 2008 and 21.4 million without employees in 2008. Small firms with fewer than 500 employees represent 99.9 percent of the total (employers and nonemployers), as the most recent data show there were 18,469 large businesses in 2008.

Source: Office of Advocacy estimates based on data from the U.S. Dept. of Commerce, Census Bureau, and trends from the U.S. Dept. of Labor, Bureau of Labor Statistics, Business Employment Dynamics.

What is small firms' share of employment?

Small businesses employ about half of U.S. workers. Of the 120.9 million nonfarm private sector workers in 2008, small firms employed 59.7 million and large firms employed 61.2 million. About half of small firm employment is in second-stage companies (10-99 employees), and half is in firms that are 15 years or older. Small firms' share of employment in rural areas is slightly higher than in urban areas; their share of part-time workers (22 percent) is similar to large firms' share (19 percent). Small firms' employment share remains steady since some small firms grow into large firms over time.

Source: U.S. Dept. of Commerce, Census Bureau: Statistics of U.S. Businesses, Current Population Survey, and Business Dynamics Statistics; and the Edward Lowe Foundation (**http://youreconomy.org**).

What share of net new jobs do small businesses create?

Small firms accounted for 65 percent (or 9.8 million) of the 15 million net new jobs created between 1993 and 2009. Much of the job growth is from fast-growing high-impact firms, which represent about 5–6 percent of all firms and are on average 25 years old.

Source: U.S. Dept. of Labor, Bureau of Labor Statistics, Business Employment Dynamics; Advocacy-funded research by Zoltan Acs, William Parsons and Spencer Tracy, 2008 (**archive.sba.gov/advo/research/rs328tot.pdf**).

How many businesses open and close each year?

An estimated 552,600 new employer firms opened for business in 2009, and 660,900 firms closed. This amounts to an annual turnover of about 10 percent. Nonemployer firms have turnover rates three times as high, mostly because it is much easier for them to go into business and cease operations.

Starts and Closures of Employer Firms, 2005–2009

Category	2005	2006	2007	2008	2009
Births	644,122	670,058	668,395	626,400e	552,600e
Closures	565,745	599,333	592,410	663,900e	660,900e
Bankruptcies	39,201	19,695	28,322	43,546	60,837

Notes: e = Advocacy estimate. Bankruptcies include nonemployer firms. Source: U.S. Dept. of Commerce, Census Bureau; Administrative Office of the U.S. Courts; U.S. Dept. of Labor, Business Employment Dynamics (BED). Estimates based on Census data and BED trends.

What is the survival rate for new firms?

Seven out of 10 new employer firms survive at least 2 years, half at least 5 years, a third at least 10 years, and a quarter stay in business 15 years or more. Census data report that 69 percent of new employer establishments born to new firms in 2000 survived at least 2 years, and 51 percent survived 5 or more years. Survival rates were similar across states and major industries. Bureau of Labor Statistics data on establishment age show that 49 percent of establishments survive 5 years or more; 34 percent survive 10 years or more; and 26 percent survive 15 years or more.

Source: U.S. Dept. of Commerce, Census Bureau, Business Dynamics Statistics; U.S. Dept. of Labor, Bureau of Labor Statistics, BED.

How are credit conditions for small firms?

Credit conditions are improving. In mid-2010, commercial banks began to ease the tight lending conditions on small businesses that had begun in early 2007. And credit has continued to flow, as loans under $1 million totalled $695 billion in FY 2009. Also, after declining over the past few years, venture capital investment dollars increased in mid-2010.

Source: Federal Reserve Board, Senior Loan Officer Opinion Survey and Call Report data; National Venture Capital Association.

Updated January 2011

How are small businesses financed?

Small businesses rely heavily upon owner investment and bank credit, averaging about $80,000 a year for young firms. Startups rely about equally on the owners' cash injections into the business and bank credit; young firms receive about three-quarters of their funds from banks via loans, credit cards, and lines of credit. One-tenth of startups and about a third of young firms do not use capital injections.

Source: Kauffman Foundation, *An Overview of the Kauffman Firm Survey: Results from the 2004–2008 Data,* (Alicia Robb, E.J. Reedy, Janice Ballou, David DesRoches, Frank Potter, Zhanyun Zhao), May 2010.

How do regulations affect small firms?

The smallest firms (fewer than 20 employees) spend 36 percent more per employee than larger firms to comply with federal regulations. The disparity is greatest in two areas: very small firms spend four and a half times as much per employee to comply with environmental regulations and three times more per employee on tax compliance than their largest counterparts.

Annual Cost of Federal Regulations by Firm Size

Type of Regulation	Cost per Employee for Firms with:		
	Fewer than 20 Employees	20–499 Employees	500 or More Employees
All Regulation	$10,585	$7,454	$7,755
Economic	4,120	4,750	5,835
Environmental	4,101	1,294	883
Tax Compliance	1,584	760	517
Occupational Safety and Homeland Security	781	650	520

Source: *The Impact of Regulatory Costs on Small Firms,* an Advocacy-funded study by Nicole Crain and Mark Crain, 2010 **(archive.sba.gov/advo/research/rs371tot.pdf)**.

Whom do I contact about regulations?

To learn about pending regulation, visit Advocacy's Regulatory Alerts webpage, **www.sba.gov/advocacy/815**; to comment on pending regulations, email **advocacy@sba.gov**. To report unfair regulatory enforcement, contact SBA's National Ombudsman at **ombudsman@sba.gov**.

What is the role of women, minority, and veteran entrepreneurs?

Of the 27.1 million nonfarm businesses in 2007, women owned 7.8 million businesses, which generated $1.2 trillion in revenues, employed 7.6 million workers, and paid $218 billion in payroll. Another 4.6 million firms were 50 percent women owned. Minorities owned 5.8 million firms, which generated $1 trillion in revenues and employed 5.9 million people. Hispanic Americans owned 8.3 percent of all U.S. businesses; African Americans, 7.1 percent; Asian Americans, 5.7 percent; American Indians and Alaska Natives, 0.9 percent; and Native Hawaiian or other Pacific Islanders, 0.1 percent. Veterans owned 2.4 million businesses in 2007, generating $1.2 trillion in receipts; another 1.2 million firms were 50 percent veteran owned. About 7 percent of veteran business owners had service-connected disabilities in 2002.

In 2008, the overall rate of self-employment (unincorporated and incorporated) was 9.8 percent, and the rate was 7.1 percent for women, 7.2 percent for Hispanic Americans, 4.7 percent for African Americans, 9.7 percent for Asian Americans and Native Americans, and 13.6 percent for veterans. Service-disabled veterans had lower self-employment rates than non-service-disabled veterans.

Source: U.S. Dept. of Commerce, Census Bureau, Survey of Business Owners; Advocacy-funded research by Open Blue Solutions, 2007 (**archive.sba.gov/advo/research/rs291tot.pdf**), and Office of Advocacy: *The Small Business Economy* (**www.sba.gov/advocacy/849**).

At what rates are the self-employed taxed?

Of the 15.5 million individuals whose primary occupation was self-employment (incorporated and unincorporated), the median personal marginal federal tax rate was 10 percent in 2008. Only 4.1 percent of the self-employed were in the marginal tax bracket of 33 percent or more.

Source: U.S. Dept. of Commerce, Census Bureau, Current Population Survey, March Supplement (special tabulation).

What research exists on the cost and availability of health insurance?

A Kaiser Family Foundation study confirmed the connection between firm size and offering health insurance. The survey shows that almost 60 percent of businesses with 3–9 workers offer health benefits to their employees. The ratio grows to more than three-fourths for firms with 10–24 employees, to 92 percent for firms with 25–49 employees, and to 99 percent for firms with 200 employees or more. Almost two-thirds of workers take health insurance coverage when offered. Overall in 2009, small firm employees were almost twice as likely as large firm employees to be uninsured (27.2 percent vs. 14.7 percent, respectively).

Source: Kaiser Family Foundation and the Health Research and Educational Trust, *Employer Health Benefits 2010 Annual Survey;* Employee Benefit Research Institute, *Sources of Health Insurance and Characteristics of the Uninsured: Analysis of the March 2010 Current Population Survey.*

How can I get more information?

For more information, visit Advocacy's website: www.sba.gov/advocacy. Specific points of interest include:

- Economic research: **www.sba.gov/advocacy/847**.
- Firm size data: **www.sba.gov/advo/849**.
- Lending: **www.sba.gov/advocacy/852**.
- Small business profiles by state and territory: **www.sba.gov/advocacy/848**.
- *The Small Business Advocate* newsletter: **www.sba.gov/advocacy/810**.

For email delivery of Advocacy's newsletter, press, regulatory news, and research, visit **http://web.sba.gov/list**. For RSS feeds, visit **www.sba.gov/advocacy/feed**. Direct questions to (202) 205-6533 or **advocacy@sba.gov**.

The SBA's Office of Advocacy was created by Congress in 1976 to protect, strengthen, and effectively represent the nation's small businesses within the federal government. As part of this mandate, the office conducts policy studies and economic research on issues of concern to small business and publishes data on small business characteristics and contributions. For small business resources, statistics, and research, visit the Office of Advocacy's home page at **www.sba.gov/advocacy**.

Frequently Asked Questions about Small Business Finance

This document sketches the ecosystem or life-cycle of small business financing. The FAQ format allows users to browse through topics and learn about specific issues. Small businesses, which include startups in such sectors as information technology, service, retail, and manufacturing, have varying financial needs. The answers provided here represent averages or totals that can be used as figures and trends for differing types of firms. For further small business data and research information, visit the Office of Advocacy's website at www.sba.gov/advocacy/847.[1]

General small business finance

What are the main reasons small businesses seek financing?

Small businesses borrow for four principal reasons: for starting the business, purchasing inventory, expanding the business, and strengthening the financials of the firm. Firms choose different means of financing depending on the intended purpose.

What types of funding do entrepreneurs and small firms use to finance their ventures?

Financing falls into two categories: **debt** and **equity**. Table 1 shows the sources and types of financing available to entrepreneurs. Some of these sources are unusual or unconventional. In addition, when a small business obtains a government procurement contract, it can play a similar role as traditional financing, providing the spark and fuel that are needed for the firm to grow.

How big is the small business financing market?

Small businesses' borrowing amounts to about $1 trillion. In 2010, the most recent year we have data for, total small business bank loans outstanding were

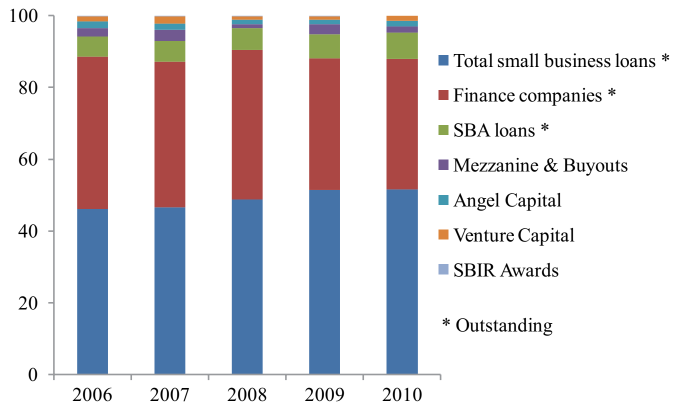
Table 1. Types of Capital by Source

Category	Source	Type
Debt	Owner(s)	Loans, bootstrapping
	Institutional lenders (banks and other depository institutions, nondepository institutions, mutual funds, pension funds, insurance companies, investment banks)	Loans, lines of credit, leases, credit cards
	Business associates	Loans, credit
	Vendor financing	Trade credit
	Family and friends	Loans
	Peer-to-peer lending	Loans
	Crowd funding	Loans
	Leasing companies	Loans, capital leases, equipment
	Brokerage firms	Loans, lines of credit
	Finance company and/or factoring	Trade credit
	Government	Loans (and loan guarantees)
	Private debt placement	Bonds
Equity	Owner(s)	Founder's capital, savings, shares
	Family and friends	Deposits, shares
	Public offering markets	Stocks
	Government:	
	Small Business Investment Company (SBIC)	Shares/ownership stake
	Small Business Innovation Research program (SBIR)	Grants
	Small Business Technology Transfer (STTR)	Grants
	Private equity placement:	
	Angel investors	Ownership stake, promissory notes
	Venture capitalists	Ownership stake, promissory notes
Hybrid	Mezzanine	Loans and/or ownership stake

Source: U.S. Small Business Administration, Office of Advocacy.
Note: For definitions, please see the glossary at the end of the FAQ.

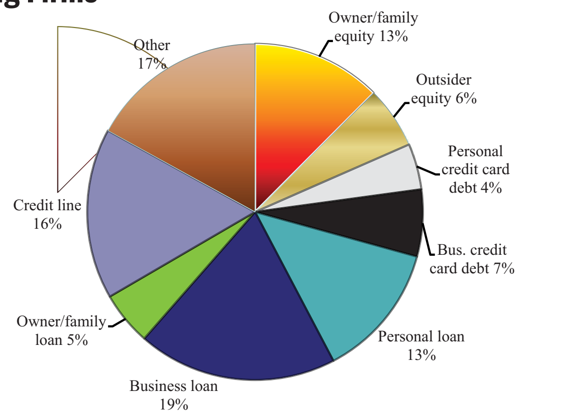
1. The data sources cited here tend to differ widely, probably because of the differing subgroups of businesses that they cover. For instance, data from the Census Bureau's Survey of Business Owners reflects all businesses, while data from D&B reflects a smaller pool dominated by older and larger businesses. This can make this FAQ seem choppy and at times inconsistent. The bottom line is that there is often no perfect data source for many of the questions.

Figure 1. Share of Financing by Category (Percent)



Note: Total small business loans are defined as all loans outstanding under $1 million, including SBA loans; SBA loans were measured as the amount outstanding at the end of the fiscal year. Finance company lending consists of all business receivables outstanding. Note that with dollar amounts being outstanding, the figures are greater than annual small business financing.

Figure 2. Share of Small Business Financing Dollars for Young Firms



Note: Firms started in 2004, reporting 2008 financing and about one-third did not use capital in the year. Source: U.S. Small Business Administration, Office of Advocacy, from data provided by Kauffman Firm Survey

valued at $652 billion, and finance companies provided another $460 billion worth of credit. All other sources combined made up around 10 percent of small business borrowing (Figure 1). The recent decline in finance company lending (another source of small business loans) is a major contributor to the tight condition of today's small business lending market. Total small business loans outstanding and SBA loans outstanding in 2010 are above 2006 levels

What share of small businesses use financing?

The answer to this question depends on whom you ask. According to the Kauffman Firm Survey, one-third of young firms do not use capital injections. Instead they rely on owner investment or nonbank sources of funds. A Census Bureau dataset finds that over half of existing firms do not need expansion financing. This reflects the fact that many businesses are not growth businesses; they reach an optimal size and stay that way. And some businesses are structured so that they self-finance. (These two sources draw from different sample pools; the Kauffman pool has a larger than average business size; the Census set includes very small businesses and its average size more closely approximates the national average.)[2]

How are small businesses financed?

For businesses that depend on financing, the two most widely used sources are owner investment and bank credit.

In their early years, young firms make heavy use of the external debt market, receiving about three-quarters of their funds from banks via loans, credit cards, and lines of credit (Figure 2). The bulk of small business financing dollars comes from business and personal loans. Outside equity, such as angel investment and venture capital, amounts to 6 percent of financing for young firms.[3]

The U.S. Census Bureau dataset confirms the importance of owner investment and bank loans, especially for employer firms (Figure 3). While the two principal financing data sources differ somewhat, similar patterns emerge from both: savings matter and bank credit matters for an important share of businesses. In addition, a significant number of established businesses do not use financing.

How are startups financed?

The Kauffman Firm Survey found that startup capital for small businesses is composed of debt and equity capital, and it averages roughly $80,000 a year per new firm. Startups depend about equally on the owners' cash injections into the business and funds from bank credit (Figure 4).[4] The most frequently used source of startup dollars was owners' and relatives' savings. The U.S. Census Bureau found that about one-third of new nonemployer firms and 12 percent of employer firms used no startup capital (Figure 5). As expected, employers made greater use of financing than did nonemployers.

What is the dollar distribution of startup financing?

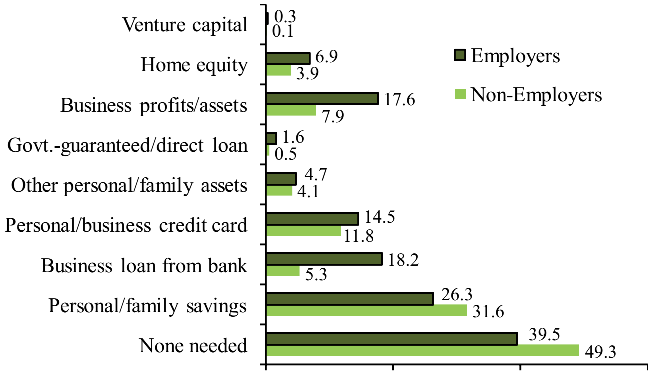
The median startup capital used by new employers is about $50,000, and by new nonemployers, $25,000. However, a large share of startups commence business operations with very little capital. A relatively large share of employers and nonemployers used less than $5,000 worth of startup financing (20 percent and 39 percent, respectively) and another sizable share did not use any startup financing (10 and 25 percent respectively). See Table 2 and Figure 5 for details.

2. The large share of businesses that use no financing is reflected in general business surveys that rank financing low on the list of pressing business concerns. Of course, for the select group of firms for whom financing is a critical need, not being able to obtain it has profound implications for their ability to expand. See National Federation of Independent Business, *Small Business Economic Trends,* www.nfib.com/research-foundation/small-business-economic-trends-sbet-archive.

3. Alicia Robb, E.J. Reedy, Janice Ballou, David DesRoches, Frank Potter, Zhanyun Zhao, *An Overview of the Kauffman Firm Survey: Results from the 2004–2008 Data,* Kauffman Foundation, May 2010. Note that results based on the Kauffman Firm Survey are based on a sample pool of businesses that are larger than the national average.

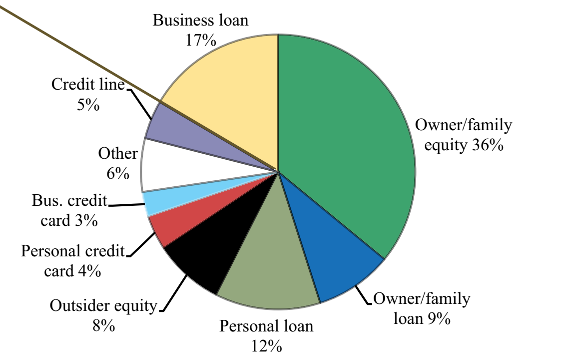
4. Alicia Robb et al., *An Overview of the Kauffman Firm Survey: Results from the 2004–2008 Data,* Kauffman Foundation, May 2010.

Figure 3. Percent of Firms Using Expansion Financing



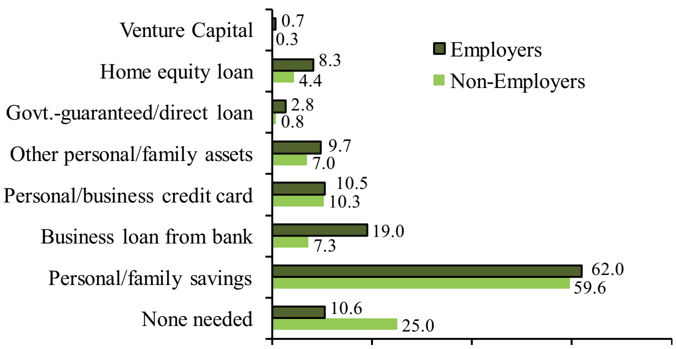
Note: Firms in existence in 2007.
Source: U.S. Small Business Administration, Office of Advocacy from data provided by the U.S. Census Bureau, Survey of Business Owners.

Figure 4. Share of Small Business Financing Dollars for Startup Firms



Note: Firms started in 2004 and about one-tenth did not use capital to start.
Source: U.S. Small Business Administration, Office of Advocacy, from data provided by Kauffman Firm Survey

Figure 5. Percent of Firms Using Startup Financing



Note: Firms in existence in 2007.
Source: U.S. Small Business Administration, Office of Advocacy from data provided by the U.S. Census Bureau, Survey of Business Owners.

Table 2: Level of Startup Capital by Firm Size (Percent)

	Employers	Nonemployers
All firms	100.0	100.0
Less than $5,000	20.3	38.7
$5,000 to $9,999	9.6	9.1
$10,000 to $24,999	13.1	8.5
$25,000 to $49,999	10.2	5.0
$50,000 to $99,999	11.5	4.1
$100,000 to $249,999	11.8	3.6
$250,000 to $999,999	7.9	2.4
$1 million or more	3.0	1.1
Not applicable	12.6	27.6

Note: Figures recalculated to account for "don't know" responses.
Source: U.S. Small Business Administration, Office of Advocacy from data provided by the U.S. Census Bureau, Survey of Business Owners.

How much do small businesses rely upon credit cards?

Credit card financing accounts for a small portion of small business capital; roughly 7 percent of all startup capital is derived from credit cards (includes personal and business credit cards). On the other hand, credit cards are very widely used. A recent study by the National Small Business Association shows the percentage of small businesses using credit cards tops all other financing choices. In a tight credit market small firms' use of credit card financing is likely to increase, especially for business expansion. Small business owners are more likely to carry credit card debt than other households (54 percent versus 45 percent respectively). With small businesses relying about half on personal credit cards and half on business credit cards, the personal credit cards would be affected by the Credit Card Act of 2009.[5]

How are franchises financed?

Existing employer franchises finance expansion using the same financial tools as other businesses, but startup franchises are more likely to use a commercial bank loan. (37.8 percent of franchises versus 23.1 percent of all employer startups used a bank loan.)[6]

5. 2009 Small Business Credit Card Survey, www.nsba.biz/docs/09CCSurvey.pdf. George Haynes, *Structure of Household Debt of Small Business Owners in the United States: Findings from the Survey of Consumer Finances, 1998–2007,* Office of Advocacy, June 2010.

6. Brian Headd and Radwan Saade, *Do Business Definition Decisions Distort Small Business Research Results?* Office of Advocacy Working Paper, August 2008.

How are veteran-owned ventures financed?

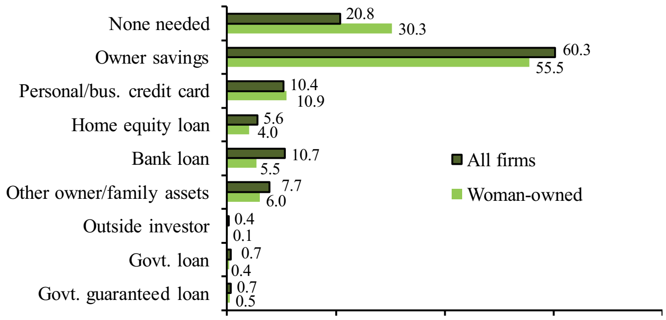
Veteran-owned businesses were extremely similar to other businesses in their use of credit for startup and expansion. For example for expansions, 11 percent of veterans used credit cards and 8 percent used bank loans while the figures were 13 percent and 9 percent, respectively, for all firms.[7]

How are women-owned ventures financed?

Women are more likely than males to start businesses without seeking financing (Figure 6). Women-owned businesses (just like their male counterparts)

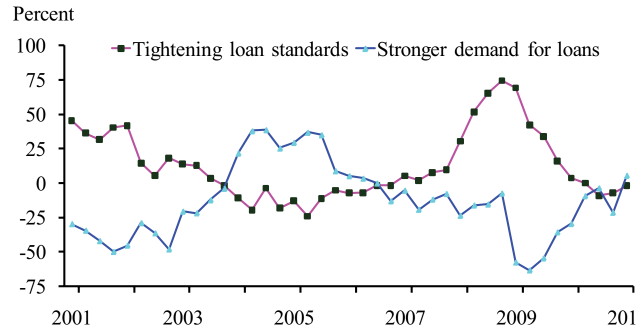
7. The data on veteran-, woman- and minority-owned firms used here come from the U.S. Census Bureau, Survey of Business Owners.

Figure 6. Types of Financing used by Woman-Owned Startups (Percent)



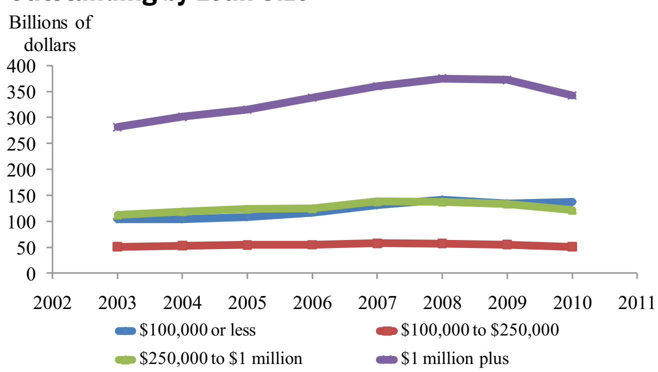
Source: U.S. Small Business Administration, Office of Advocacy from data provided by the U.S. Census Bureau, Survey of Business Owners.

Figure 7. Small Business Bank Lending



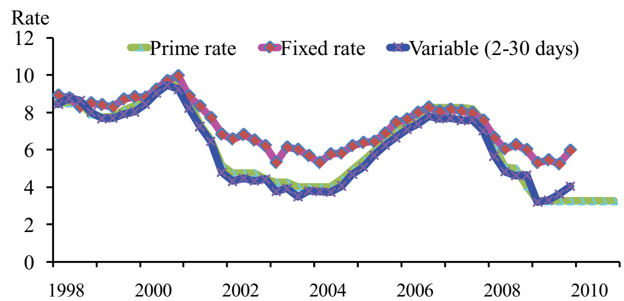
Note: Change in percentage of respondents from the previous period.
Source: Office of Advocacy, U.S. Small Business Administration from data provided by the Federal Reserve Board Senior Loan Officer Survey.

Figure 8. Commercial and Industrial Loans Outstanding by Loan Size



Source: Office of Advocacy, U.S. Small Business Administration from data provided by the Federal Reserve Board Call Report data.

Figure 9. Small Business Interest Rates (Loan size $100,000 to $499,000)



Source: Office of Advocacy, U.S. Small Business Administration from data provided by the Federal Reserve Board, Survey of Terms of Lending.

largely depend on personal finances; they are more likely to use credit cards to fund their businesses. And women are almost half as likely as male-owned businesses to obtain business loans from banks. This puts women-owned businesses at a disadvantage, because a business's relationship with a bank at the outset not only provides funds, but often provides business advice and future goodwill.

How are minority-owned ventures financed?

At startup, Hispanic-owned firms are less likely than other business owners to have bank loans. Firms owned by Hispanic-Americans, African-Americans, and Asian-Americans were more likely to rely on credit cards at the outset. When expanding, Hispanic-owned firms and African-American owned were more likely to rely upon credit cards than other firms. This heavier-than-average reliance on credit cards negatively affects a business by displacing a personal relationship with a bank, which is often the source of less costly financing that is tailored to a business's needs.

How does the debt held by small business-owning households differ from other households' debt?

Small business-owning households held 59 percent of their debt in mortgages, versus 38 percent for other households. They were even further dependent on real estate as they held another 7 percent of their debt in residential secured debt.[8] This dependence on real estate illustrates the double storm that small businesses have weathered in the last few years of declining real estate values and tight credit in financing their businesses.

8. George Haynes, *Structure of Household Debt of Small Business Owners in the United States: Findings from the Survey of Consumer Finances, 1998–2007,* Office of Advocacy, June 2010.

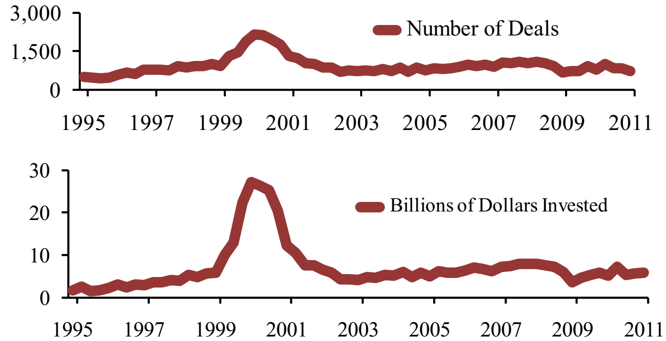
Current environment

What is the current lending environment for small businesses (as of August 2011)?

Credit conditions in the small business market continue to remain tight, even though commercial banks began easing lending conditions in mid-2010 (Figure 7). Billions of dollars outstanding for all loan sizes are down from pre-recessionary levels. But bank loans under $1 million held relatively steady during the downturn, while larger loans ($1 million or more) saw a pronounced decline (Figure 8).[9]

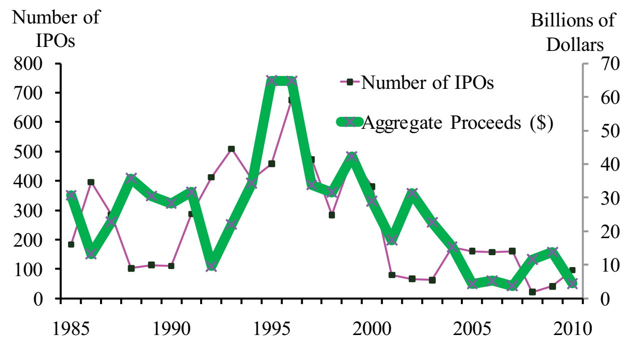
9. Federal Reserve Board, Senior Loan Officer Opinion Survey and Call Report data.

Figure 10. Venture Capital



Source: Office of Advocacy, U.S. Small Business Administration from data provided by PricewaterhouseCoopers/National Venture Capital Association using Thomson Reuter data.

Figure 11. Initial Public Offerings



Source: Office of Advocacy, U.S. Small Business Administration from data provided by Prof. Jay R. Ritter, University of Florida.

What interest rates are small businesses typically charged for loans?

Fixed interest rates on loans between $100,000 and $499,999 have been 6 percent while short-term variable rate loans (2-30 days) have been about 4 percent (Figure 9). While interest rates are near their lowest point in a decade, in 2009 the spread between the prime rate and the variable interest rate increased; this represents a perceived risk in small business lending not seen in the previous downturn around 2000. Interest rates on credit card balances vary widely.

What is the status of the venture capital market?

The venture capital market is down substantially in both deals and dollars from the bubble of 1999-2001 (Figure 10). More importantly, the steady growth in deals and dollars that existed in the late 1990s has not resumed. The venture capital markets have been flat for nearly a decade since the bubble burst. However, venture capital is also about 30 percent below pre-recession levels in the number of deals and dollars.

What is the status of the initial public offering market?

While the number of initial public offerings (IPOs) has risen since 2008, the 2000s could be considered a lost decade of IPOs; their number and value relative to the 1990s declined significantly (Figure 11). The IPO market has been on a roller coaster ride over the past two decades; a healthy IPO market is probably in the range of 250-350 deals per year, a level which has not been seen since 2000. The trends in aggregate proceeds seem to mirror the trends in the number of IPOs although one could argue that dollars have lagged listings by a few years (Figure 11).

What is the condition of the angel capital market?

Accredited investors, also known as angels, are investors who are qualified based on federal securities laws. The angel market was down in 2008 and 2009, but was revived in 2010 with increases of 14 percent in dollars invested and 8.2 percent in the number of entrepreneurial ventures that received angel funding. But the angel market for seed and startup capital continues to contract as angels shift their preference to later-stage investments (post-seed/startup investments).[10]

How did the downturn affect business lending by large and small banks?

Large bank lending tends to follow the business cycle while smaller bank lending tends to be relatively steady. Banks with $50 billion or more in assets had solid increases in their commercial and industrial lending (outstanding) from 2003 to 2008 and had declines in 2009 and 2010 because of the downturn (Figure 12). Most other bank sizes had relatively flat lending trends during this time period, with the exception of the smallest banks. Lending at these banks (with less than $100 million in assets) has been in a long-term declining trend. While smaller banks might be seen as a shock absorber for small business financing during a downturn (since their lending held steady), their minimal growth in lending over nearly a decade could also be an indicator of their waning ability to be a small business resource.

What is the approval rate of small business loans?

In the first quarter of 2010, Biz2Credit reports that slightly less than half of all small business loans were approved (www.biz2credit.com).

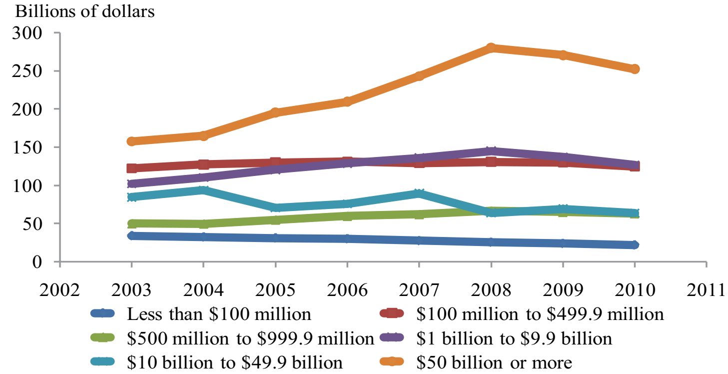
Government financing

What are SBA loans?

SBA loans are government-backed loans available through commercial lenders which follow SBA's guidelines. Except for the disaster loan program (www.sba.gov/taxonomy/term/99), the SBA does not make direct loans to small businesses. SBA works with lenders to provide a partial guarantee for loans. In essence, SBA acts like a co-signer for small businesses who often lack collateral or a credit history. SBA's partial guarantee reduces the risks for lenders, increases lending to small business, and allows small businesses to expand economic activity. From a policy perspective, SBA's costs for such programs are loan

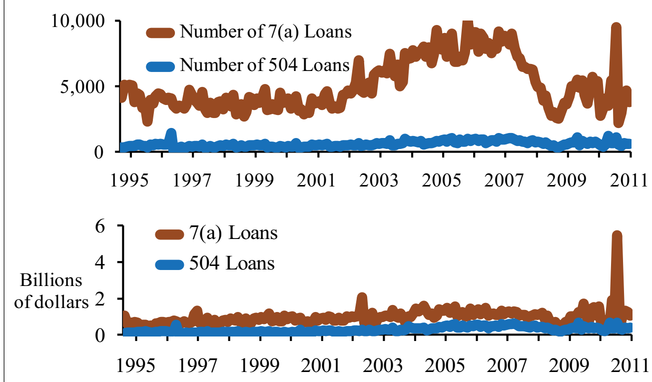
10. University of New Hampshire, Whittemore School of Business and Economics, Center for Venture Research.

Figure 12. Commercial and Industrial Loans Outstanding By Bank Asset Size



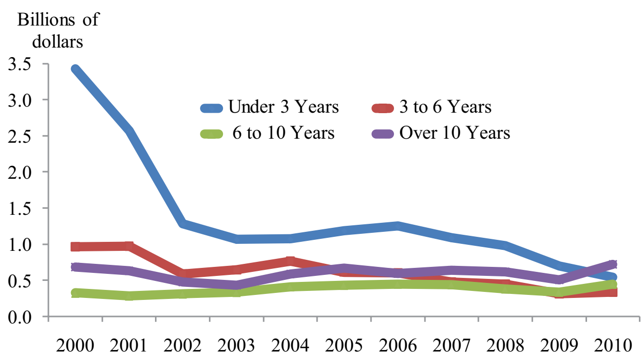
Source: Office of Advocacy, U.S. Small Business Administration from data provided by the Federal Reserve Board CRA data.

Figure 13. SBA Loans



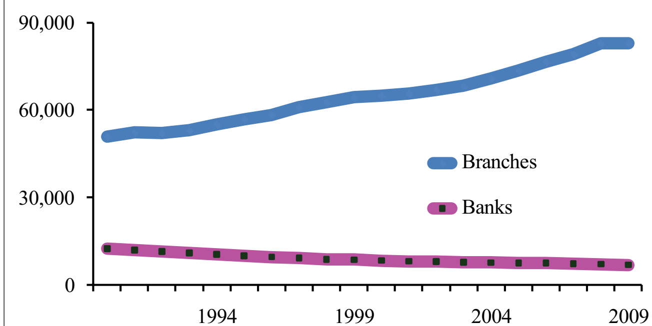
Source: U.S. Small Business Administration.

Figure 14. SBIC Funding by Age of Firm



Source: U.S. Small Business Administration.

Figure 15. Number of Lending Institutions



Source: Office of Advocacy, U.S. Small Business Administration from data provided by the FDIC.

losses minus fees, not the entire amount that SBA guarantees, as loans are to be repaid. For more information about SBA loan programs, see www.sba.gov/category/navigation-structure/loans-grants/small-business-loans.

How has the business cycle affected SBA loans?

While the economic downturn has substantially affected the number of SBA loans, the dollar amount has changed less. In some ways SBA loans are a shock absorber in times when credit is tight, but even this program is not immune to the economics of decreased loan demand in the peak and nadir of a downturn. Making the data difficult to interpret is the fact that SBA guarantees and fees have changed over the years; this creates various pullbacks and surges in the SBA loan program such as the spike in lending at the end of 2010 (Figure 13).

Can a small business obtain financing after a natural disaster?

Depending on the viability of the small business in the aftermath of a natural disaster, the SBA may be able to make a direct low-interest, long-term loan to repair physical and economic damage caused by a declared disaster. For details see www.sba.gov/category/navigation-structure/loans-grants/small-business-loans/disaster-loans.

What are Small Business Investment Companies and whom do they fund?

Small Business Investment Companies (SBICs) are privately owned and managed investment funds, licensed and regulated by SBA. SBICs combine their own capital with SBA-guaranteed funds to make equity and debt investments in qualifying small businesses.

Small businesses can seek funds from SBICs at different stages of development, but note that at the beginning of the decade SBICs were more likely to fund startups, and have shifted to mature companies in recent years (Figure 14).

Are there other federal government programs for small businesses?

Yes, one such program is the Department of Agriculture's B&I Guaranteed Loan Program, whose structure is similar to SBA loan guarantees. For details see www.rurdev.usda.gov/rbs/busp/b&i_gar.htm. The Department of Treasury's Community Development Financial Institutions Fund also helps promote access to capital in urban and rural low-income communities (www.cdfifund.gov).

Two additional programs, Small Business Innovation Research (SBIR) and Small Business Technology Tranfer (STTR), offer research and development grants and contract opportunities targeted to small businesses.These are perhaps the best sources of risk capital available to fund the development of promising new technologies. SBA does not administer awards, but has the responsibility for directing the participating agencies in the administration of the program.[11]

Policy issues

How has the Sarbanes–Oxley Act of 2002 affected small businesses?

The Sarbanes–Oxley Act mainly applies to publicly traded companies with a public float of $75 million and above. Most small businesses are privately held or below this threshold, but the law could require them to be audited if they are suppliers to publicly traded companies. While certain small businesses are subject to the law, the overall small business impact is unclear and is likely to remain so until sufficient data becomes available to evaluate.

How has bank consolidation affected small businesses?

Bank consolidation affects small business loan markets differently depending on the degree of competition in these markets. Proving how this affected small business lending is difficult because of the uncertainty in developing a scenario where the banks would not have merged at such high rates. And research has shown that the availability of credit to most small firms has not been adversely affected by large bank mergers and acquisitions.12 The number of lending institutions has declined almost 50 percent in the past two decades (Figure 15). A separate, encouraging trend is that the number of bank branches has increased by almost two-thirds during the same period, providing more opportunities for small businesses to maintain local banking relationships.

Research and data sources

Where can I obtain small business data on financing?

The U.S. Census Bureau's *Statistical Abstract of the United States* is a good starting point for summary financing statistics (www.census.gov/compendia/statab/cats/banking_finance_insurance.html). Additionally, data aggregators such as the Federal Reserve Bank of St. Louis's FRED (http://research.stlouisfed.org/fred2) and the Federal Government's Data.Gov (www.data.gov) can in some cases provide one-stop data shopping. However, much of the data discussed in the *Stat Abstract* is not related to small business, so most researchers will have to access microdata (i.e., records for individual businesses sans personal information) and/or aggregated business data from the following sources.

The business financing data sources which contain microdata are:

- The Kauffman Firm Survey or KFS (Kauffman Foundation, www.kauffman.org/kfs);
- EDGAR, the Securities and Exchange Commission's database of publicly traded companies (www.sec.gov/edgar.shtml);
- The Panel Study of Entrepreneurial Dynamics (www.psed.isr.umich.edu/psed); and
- The defunct Survey of Small Business Finances or SSBF (Federal Reserve Board, www.federalreserve.gov/pubs/oss/oss3/nssbftoc.htm).
- Note that the Survey of Consumer Finances also contains limited small business financing data (Federal Reserve Board, www.federalreserve.gov/pubs/oss/oss2/scfindex.html).

KFS followed about 5,000 startups in 2004 to 2009 with plans to follow them through 2011. EDGAR has filing information on publicly traded companies. PSED contains about 800 businesses followed from 1998 to 2000 with three follow-ups up to 2006. SSBF contains about 4,000 data points for the years, 1987, 1993, 1998, and 2003. These micro datasets contain a wealth of variables and are useful in determining how various business types are financed and, in some cases, could allow the researcher an opportunity to show their impact on the firm.

Aggregated financing figures contain limited variables but are helpful in showing financing trends through historical data. Data sources publishing aggregate business financing figures include:

- The Senior Loan Officer Survey (SLOS, Federal Reserve Board, quarterly, www.federalreserve.gov/boarddocs/snloansurvey);
- Call Reports (Federal Deposit Insurance Corporation, quarterly, https://cdr.ffiec.gov/public);
- Community Reinvestment Act filings (Federal Financial Institutions Examination Council, annual, www.ffiec.gov/cra/craproducts.htm);
- Initial public offerings (Prof. Jay Ritter, University of Florida, http://bear.warrington.ufl.edu/ritter/ipodata.htm);
- Venture capital statistics (PricewaterhouseCoopers/National Venture Capital Association using Thomson Reuter data, annual and quarterly, www.nvca.org);
- Survey of Business Owners (U.S. Census Bureau, quinquennial, www.census.gov/econ/sbo/02/cbsof.html); and
- Small Business Loan data (U.S. Small Business Administration, weekly, www.sba.gov/category/lender-navigation/lender-loan-data).

Some sources, such as the Flow of Funds report, include small businesses but they are overwhelmed by data for large businesses (Federal Reserve Board, quarterly, www.federalreserve.gov/releases/z1/default.htm).

Although the Office of Advocacy does not endorse them, a few commercial subscription data sources are available and contain microdata. These can be used to gather small business finance information for individual companies or aggregate figures.

---

11. Federal agencies with annual research and development budgets exceeding $100 million are required to allocate a portion of their R&D budget to these programs. Currently, 11 federal agencies participate in the program: the Departments of Agriculture, Defense, Education, Energy, Health and Human Services, Homeland Security, and Transportation; the Department of Commerce's National Institute of Standards and Technology and National Oceanic and Atmospheric Administration; Environmental Protection Agency; National Aeronautics and Space Administration; and National Science Foundation

12. Charles Ou, *Banking Consolidation and Small Business Lending: A Review of Recent Research,* Office of Advocacy, March 2005.

These sources include:

• ABI/Inform (www.proquest.com/en-US/catalogs/databases/detail/abi_inform.shtml);

• Center for Research in Security Prices (www.crsp.com);

• Compustat (www.compustat.com/compustat_data);

• D&B (www.dnb.com);

• Experian (www.experian.com); and

• Hoover's (www.hoovers.com).

Unanswered questions

Frequently asked questions that remain unanswered.

Some questions remain very hard to answer, primarily because of a lack of data. They include:

What is the default rate of small business loans?

Is there a "valley of death" or "capital chasm," i.e., a middle level of financing that is a barrier to growing firms?

How much capital do small businesses receive from finance companies?

How do small businesses spend the financing funds they receive?

How many small business owners have personal guarantees on their loans?

What dollar amount of small business loans do banks charge off each year because of nonperformance?

What is small businesses' creditworthiness, how does it compare to large firms' creditworthiness and how is this affected by the business cycle?

Additional Publications

Small Business in Focus: Finance. U.S. Small Business Administration, Office of Advocacy, www.sba.gov/sites/default/files/09finfocus_0.pdf;

"Financial Services Used by Small Businesses: Evidence from the 2003 Survey of Small Business Finances" by Traci L. Mach and John D.Wolken. Federal Reserve Board, *Federal Reserve Bulletin,* October 2006;

"Women and Men Entrepreneurs: Different Relationships to Bootstrap Finance" by Lynn Neeley and Howard Van Auken. *Journal of Developmental Entrepreneurship*, 2010.

"Five Unique Loan Sources," NFIB www.nfib.com/business-resources/business-resources-item?cmsid=49178.

Glossary

Angel investor. An individual or accredited investor who provides early stage funding, and are known to invest their own money rather than that of an institution.

Bootstrapping/bootstrap financing. The actions of a startup to minimize expenses and build cash flow, thereby reducing or eliminating the need for outside investment.

Crowd funding. (Sometimes called crowd financing or crowd-sourced capital.) A collective cooperation of people who network and pool their money and resources together, usually via the Internet, to support efforts initiated by other organizations. While peer-to-peer lending typically focuses on one individual lending to another, crowd funding—as its name implies—aims to reach a funding goal by aggregating many small investors.

Factoring. A financial transaction whereby a business sells its accounts receivable (i.e., invoices) to a third party (called a factor) at a discount in exchange for immediate money with which to finance continued business operations.

Loans outstanding. The unpaid balance on any term loan, installment, revolving or credit card debt on which interest is charged.

Mezzanine financing. A hybrid of debt and equity financing that is typically used to finance the expansion of existing companies—the debt capital gives the lender the rights to convert to an ownership or equity interest in the company if the loan is not paid back on time and in full. Mezzanine debt is typically senior to original equity invested in the company, but junior to any bank financing. In essence, the mezzanine financing fills in the gap between the first mortgage held by a bank and the equity contributed by the principal owners of the business.

Peer-to-peer (P2P) lending. A lending arrangement in which individuals with little or no collateral seek loans from ordinary people looking to lend (via an online social lending marketplace/network); lenders compete with each other to make loans, often resulting in lower rates for the borrowers.

Small Business Investment Company (SBIC). A company licensed by the Small Business Administration to receive government capital in the form of debt or equity to use in private equity investing.

Small Business Innovation Research program (SBIR). A federal program awarding research and development funds to small businesses to develop and commercialize new technologies.

Small Business Technology Transfer (STTR). A federal program fostering innovation by funding small business research and development and developing public/private partnerships among small businesses and nonprofit research institutions.

Trade credit. A business-to-business arrangement in which a supplier provides goods and services at one point in time and collects the charges at a later point. Put another way, receiving a discount for paying early is equivalent to being charged interest for paying later.

Vendor financing. A loan from one company to another which is used to buy goods from the company providing the loan.

Venture Capital. A segment of the private equity industry often investing in high risk/high growth companies with pooled funds, sometimes from large institutions.

About the Office of Advocacy

The SBA's Office of Advocacy was created by Congress in 1976. Part of the office's mission includes conducting policy studies and economic research on issues of concern to small businesses. The office also publishes data on small firm characteristics and contributions. For further data and research information, visit the Office of Advocacy's website at www.sba.gov/advocacy/847.